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Supreme Court of the United States.

October Term, 1935.

No. 125.

PALMER CLAY PRODUCTS COMPANY,
Petitioner,

v.

MATTHEW BROWN, Trustee in Bankruptcy of Metropolitan Builders Supply Company,
Respondent.

Brief for Respondent in Opposition to Petition for Writ of Certiorari.

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Supreme Court of the United States.

OCTOBER TERM, 1935.

No. 125.

PALMER CLAY PRODUCTS COMPANY, *Petitioner*,

v.

MATTHEW BROWN, TRUSTEE IN BANKRUPTCY OF METROPOLITAN BUILDERS SUPPLY COMPANY, *Respondent*.

BRIEF FOR RESPONDENT IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

Statement of the Case.

The facts involved in this petition for a writ of certiorari to the Municipal Court of the City of Boston, County of Suffolk, Commonwealth of Massachusetts, are set forth in the record, and may, we believe, be briefly stated as follows:

The petitioner, on or about November 8, 1932, was a creditor of the Metropolitan Builders Supply Company in the sum of $2088.29 for merchandise, all of which was sold by the petitioner to the Metropolitan Builders Supply Company at various times prior to that date, no merchandise having been sold by the petitioner subsequent to November 8th. (See Transcript of Record, page 11, line 10.) Between November 8, 1932, and January 3, 1933, the petitioner received in full payment of its balance due the sum of $2088.29, receiving $1688.29 from the Metropolitan Builders Supply Company and $400 on December 5, 1932, from the firm of Louis B. Cadario & Sons, a third party from whom

the petitioner had received a guarantee of the account at a prior date, the said guarantor having received no security or right to any of the assets of the said Metropolitan Builders Supply Company for the giving of said guarantee to the petitioner.

The trial justice of the Municipal Court of the City of Boston, after hearing the case, on December 15, 1933, found for the respondent, and made the following findings of fact:

> "I find that on November 8, 1932, and thereafter, the defendants had reasonable cause, 1st, to believe that the Metropolitan Builders Supply Company was insolvent, and 2nd, that payments made thereafter to them by the said Metropolitan Builders Supply Company would effect a preference over other creditors of the same class. I find that the payments made by the guarantors on December 6, 1932, and December 14, 1932, were not preferential payments." (See Transcript of Record, page 13. See also subsequent amendment of finding increasing amount—Transcript of Record, page 13.)

The trial justice denied request for ruling No. 8 of the petitioner, which was as follows:

> "The burden is on the plaintiff to prove that each of the payments received by the defendant had the effect of enabling the defendant to receive a greater percentage of its claim than other creditors of the same class could at the time of each payment have received." (See Transcript of Record, page 19.)

Following the above finding, the petitioner requested the Appellate Division of the Municipal Court of the City of Boston to report the case to the Supreme Judicial Court of Massachusetts. The request for report was dismissed

by that court, after hearing, on May 16, 1934. (See Transcript of Record, page 5.) Thereupon, the petitioner filed his claim of appeal from this ruling to the Supreme Judicial Court of the Commonwealth of Massachusetts. That court, after hearing, sustained the ruling of the Appellate Division, and on the 6th day of March, 1935, rescript was received by the Municipal Court of the City of Boston from the Supreme Judicial Court in the following words, to wit:

> "ORDERED, that the Clerk of said Court in said County make the following entry under said case in the docket of said Court, viz:—
>
> Order dismissing report affirmed.
>
> By the Court,
>
> March 5, 1935. WALTER F. FREDERICK, Clerk."

(See Transcript of Record, bottom of page 5 and top of page 6.)

Statement of the Issues.

The sole question presented to the Supreme Judicial Court of Massachusetts by the petitioner on appeal was the correctness of the refusal of the trial justice to grant its request for ruling No. 8. It was the petitioner's contention that, while the Supreme Court of Massachusetts had decided this question adversely to it in accordance with its ruling in the case of *Rubenstein* v. *Lottow*, 223 Mass. 227, the refusal to grant this request was in conflict with the law as apparently set forth in certain Circuit Court of Appeals decisions of the Eighth Circuit. The petitioner now predicates his prayer to this court that a writ of certiorari issue to the Municipal Court of the City of Boston on the same ground, stating that the issues are as follows:

> "(1) Whether the preferential character of a transfer of property is to be determined as of the date of the

actual transfer, or as of some future time, viz., the time of the filing of the petition in bankruptcy.

"(2) What is the test to be applied in determining whether a creditor, who is alleged to have received a preferential transfer, has received a greater percentage of its debt than other creditors of the same class.

"(a) What percentage creditors of the same class would have received at the date of the actual payment or transfer, or

"(b) What other creditors of the same class received at some future time, viz., the time of the filing of the petition in bankruptcy or final administration of the bankrupt estate.

"(3) Whether or not the Massachusetts State Courts acted erroneously in refusing the petitioner's request for ruling of law, which was as follows:—

" 'The burden is on the plaintiff to prove that each of the payments received by the defendant had the effect of enabling the defendant to receive a greater percentage of its claim that other creditors of the same class could at the time of each payment have received.' "

The pertinent sections of the Bankruptcy Act, Act of July 1, 1898, c. 541, 30 U.S. Sts. at Large, 544, 562, as amended by Act of February 5, 1903, 32 U.S. Sts. at Large, 799, c. 487, sec. 13, and by Act of June 25, 1910, 36 U.S. Sts. at Large, 842, c. 412, sec. 11, which are called in question are as follows:

"Sec. 60, Preferred Creditors.

"(a) A person shall be deemed to have given a preference, if, being insolvent, he has, within four months before the filing of the petition, or after the filing of the petition and before the adjudication pro-

cured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class. Where the preference consists in a transfer, such period of four months shall not expire until four months after the date of recording or registering of the transfer, if by law such recording or registering is required or permitted.

"(b) If a Bankrupt shall have procured or suffered a judgment to be entered against him in favor of any person or have made a transfer of any of his property, and if, at the time of the transfer, or of the entry of the judgment, or of the recording or registering of the transfer if by law recording or registering thereof is required, and being within four months before the filing of the petition in bankruptcy or after the filing thereof and before the adjudication, the bankrupt be insolvent and the judgment or transfer then operate as a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall then have reasonable cause to believe that the enforcement of such judgment or transfer would effect a preference, it shall be voidable by the trustee and he may recover the property or its value from such person. And for the purpose of such recovery any court of bankruptcy, as hereinbefore defined, and any state court which would have had jurisdiction if bankruptcy had not intervened, shall have concurrent jurisdiction."

Briefly stated, the respondent submits that the first issue before the court is a preliminary issue as to jurisdiction, as follows:

Was the petition for certiorari to the Municipal Court of the City of Boston, applied for in this court, filed by the petitioner within the three-months period as required by the Act of September 6, 1916, c. 448, 39 Stat. pp. 726, 727, and 728, which is as follows:

> "No writ of error, appeal, or writ of certiorari intended to bring up any cause for review by the Supreme Court shall be allowed or entertained unless duly applied for within three months after entry of judgment or decree complained of."

The remaining issues, on the merits, the respondent submits are as follows:

1. It is not open to the petitioner to argue to this court that the findings of the trial justice were not supported by the evidence.

2. The trial court's findings of fact as supported by the evidence appearing in the record before this court rendered the petitioner's request for ruling No. 8 immaterial, and therefore the ruling by the trial justice refusing to grant this request, even if it were an erroneous ruling, was not prejudicial to the petitioner, and gives him no right to a review of the question of law presented by this request for ruling.

3. The decision of the Supreme Judicial Court of Massachusetts in this case was in accordance with the spirit and purpose of the Bankruptcy Act, and is supported by decisions of this court and the weight of authority in the United States District Courts, Circuit Courts of Appeals, and the highest courts of the states.

4. The decision of the trial court being supported by the evidence, regardless of the ruling made by the trial court on request for ruling No. 8 of the petitioner, and the decision of the Supreme Judicial Court of Massachusetts having been a correct interpretation of the Bankruptcy

Act, sections 60*a* and 60*b* as sustained by the weight of authority, this court in the exercise of its discretion should refuse to take jurisdiction by certiorari.

Jurisdiction.

THE RESPONDENT SUBMITS THAT THE PETITIONER HAS FAILED TO APPLY FOR WRIT OF CERTIORARI WITHIN THE TIME GRANTED TO HIM BY THE ACT OF SEPTEMBER 6, 1916, CHAPTER 448.

It would appear clear that no petition for certiorari to this court can be applied for until the last step which can be taken in the inferior courts has been disposed of and the case finally determined in the court of last resort in the jurisdiction to which the petitioner is requesting certiorari to issue.

The respondent submits, however, that when such final proceeding has terminated, the three-months period within which certiorari must be applied for then commences, and that the date from which the three-months period is computed is the date of that final decision of the highest tribunal, and from no other date.

The course of the litigation in the state courts of Massachusetts in this case terminated by the refusal of the Supreme Judicial Court on March 5, 1935, to grant to the petitioner its appeal from the ruling of the Appellate Division of the Municipal Court of the City of Boston, County of Suffolk, State of Massachusetts, refusing its request for a report to the Supreme Judicial Court. This was a finding on the merits. On March 6, 1935, rescript was received from the Supreme Judicial Court in the following words:

> "ORDERED that the Clerk of said Court in said County make the following entry under said case in the docket of said Court, viz:—
>
> "Order dismissing report affirmed."

By this order, the highest tribunal of Massachusetts to which the petitioner had final right of appeal terminated the course of this litigation.

That the petitioner himself regarded this finding as the conclusion of the litigation is established by the fact that on the 7th day of March, 1935, the day following the entry of the order, the petitioner gave notice to the respondent of a motion to be argued before the Municipal Court of the City of Boston on the 11th of March, 1935, in which he moved "that the issuance of execution therein be stayed pending petition to the Supreme Court of the United States for writ of certiorari to review the judgment of this Court entered in this case." (See Transcript of Record, page 6.)

It will appear from the Transcript of the Record (see page 6) that the order of the Supreme Judicial Court denying the petitioner's appeal is the final entry in the docket of the Municipal Court of the City of Boston apart from the motion to stay execution and order entered thereon, although the petitioner in his brief refers to the date of "Final Judgment" as being March 15, 1935. Even assuming that such an entry appears on that date in the docket of the Municipal Court of the City of Boston and is not disclosed by the record, the respondent submits that this date has no bearing on the question as to when the three-months period within which a writ of certiorari must be applied for commences.

It would indeed be a curious Statute of Limitations which required for its commencement the doing of a clerical act which would be subject to the delay, negligence, illness, or any of the other numerous factors which enter into the mere clerical docketing of an order in the records of the trial court. It would, however, appear clear that the date on which the final order is made by the highest tribunal of the jurisdiction appealed from is of such definite character as to time

and of such finality as to character as to be the proper date to commence reckoning the three-months period.

This court seems to have so held in the case of *Andrews* v. *Virginian Railway Co.*, 248 U.S. 272. In that case the respondent argued that the period must commence from the date when judgment was originally issued by the trial court despite the fact that the petitioner had further courses open to it in the state courts to appeal from said judgment. This court decided that the period commenced upon the decision of the highest tribunal on appeal from the original judgment.

In this case the respondent is not contending that the three-months period should have commenced with the 13th day of January, 1934, on which date the Municipal Court of the City of Boston made its finding for the respondent in the sum of $1688.29, with interest. He does contend, however, that, in accordance with the ruling in the case of *Andrews* v. *Virginian Railway Co.* (see *supra*), the last appeal from this finding having terminated on March 6, 1935, the three-months period within which to apply for certiorari then commenced.

In *Citizens' Bank of Michigan City, Indiana,* v. *Opperman,* 249 U.S. 448, this court stated that, when a petition for rehearing is entertained in the state court, the judgment does not become final for the purpose of review to the United States Supreme Court until the petition has been denied, or otherwise disposed of, and the three-months period begins to run from that time.

Again in *Chicago Great Western Railroad Co.* v. *Basham, Administrator of Spellman,* 249 U.S. 164, the court said that the "Judicial Code permits review by this court only of the final judgment or decree of the highest court in which a decision in the suit could be had. It is only a judgment marking the conclusion of the course of litigation in the courts of the State that is subject to our review.

Hence, whatever its form of finality, if a judgment be in fact subject to reconsideration and review by the State Court of last resort through the medium of a petition for rehearing and such petition is presented to and considered by that Court we must take it that by the practice prevailing in the State, the litigation is not brought to a conclusion until this petition is disposed of and until then the judgment previously rendered cannot be raised as a final judgment within the meaning of the Act of Congress."

The respondent submits that the decisions of this court in the cases heretofore cited indicate that the finding of the trial justice of the Municipal Court of the City of Boston on the 13th day of January, 1934, became final on March 6, 1935, on which date the Supreme Judicial Court, the highest tribunal to which the petitioner could appeal from the trial court's finding, affirmed the decision of the Appellate Division dismissing the request for a report. The petitioner therefore submits that the three-months period within which application for certiorari could be made to this court commenced on March 6, 1935, and that this three-months period elapsed on June 6, 1935.

The record in this case will indicate that the petition and supporting brief were not filed by the petitioner with the Clerk of this Court until the 13th day of June, 1935, and that it is therefore late.

If it be true that the petition was filed late, then it cannot be entertained by this Honorable Court even if the record should indicate (although your respondent says that it does not) a proper case for allowance, and therefore this petition for certiorari should be denied.

Rust Land Co. v. *Jackson,* 250 U.S. 71, at 76.

Argument on the Merits.

I.

IT IS NOT OPEN TO THE PETITIONER TO ARGUE TO THIS COURT THAT THE FINDINGS OF THE TRIAL JUSTICE WERE NOT SUPPORTED BY THE EVIDENCE.

Apart from the jurisdictional objection to this petition for certiorari as heretofore set forth, the respondent submits that the only possible basis for a rehearing of this case by this court which can be urged by the petitioner must rest on the question of the correctness of the denial by the trial justice of its request for ruling No. 8, and that at this stage of the proceedings it cannot inject any argument in support of the petition for certiorari to the effect that the evidence submitted to the trial court did not support the findings made.

On page 2, paragraph 3, of the petition for certiorari and brief in support thereof filed by the petitioner the petitioner attempts to do this very thing and would argue at this date, for the first time, that it was a secured creditor having a guarantee from a third person, that no evidence was introduced as to what percentage of their claims could be paid to all creditors of the petitioner's class on the dates when the various payments were made, nor as to what dividends were paid to creditors generally.

It was open to the petitioner in the state court by a proper request for ruling or exception to the findings of fact to present these issues to an appellate court. Not having done so, it was not open to the petitioner, even in the state court, to take exceptions to the findings of fact of the trial justice.

Reid v. *Doherty*, 273 Mass. 388.
Richards v. *Appley*, 187 Mass. 521.

In the latter case the Supreme Court of Massachusetts stated: "If no ruling was asked for on the evidence, it is too late to except to a finding on the ground that it is not warranted by the evidence."

And it is clearly not open to the petitioner to argue in this court that the findings of fact in the trial court were not supported by the evidence.

In the case of *Eau Claire National Bank* v. *Jackman, Trustee in Bankruptcy,* 204 U.S. 522, suit was brought by a trustee in bankruptcy to recover a preference from the Eau Claire National Bank. The issues raised were almost on all fours with the ones here raised by the petitioner. The trial court found as a fact that certain transfers of property were made to the bank by the bankrupt; that it was the intention of the bankrupt to give a preference; that the bank when receiving the preferential payments had reasonable cause to believe that the bankrupt intended to give such a preference "to enable it to obtain a greater percentage of its indebtedness than any other of his [the bankrupt's] creditors of the same class would be enabled to obtain." The petitioner attempted in this court to raise, among other issues, the question as to what class of creditors the bank belonged and certain other questions of fact. This court refused to consider such assignments of error, stating:

> "On the merits of the case we start with the facts established against the bank that the property of Young [the bankrupt] at the time he executed the chattel mortgages and when he executed the deed to the lumber company, at a fair valuation, was insufficient to pay his debts and that by execution of these instruments and by the transfer of his property effected thereby, he intended to give the bank a preference over his other creditors, and that the bank had rea-

sonable cause to believe that he intended thereby to give it a preference and to enable it to obtain a greater percentage of its debt than any other creditors of Young of the same class. These then are the prominent facts and seemingly justified the judgment."

So here, the trial court having found as a fact that "on November 8th, 1932, and thereafter, the defendants had reasonable cause, 1st, to believe that the Metropolitan Builders Supply Company was insolvent, and 2nd, that payments made thereafter to them by the said Metropolitan Builders Supply Company would effect a preference over other creditors of the same class," every element necessary to establish a preference having been found as a fact, the judgment would seemingly be justified.

See *Dutcher* v. *Wright*, 94 U.S. 553, at 557.

Even if it is granted for the purposes of argument that it is still open to the petitioner to make the arguments set forth in its supporting brief on page 2, paragraph 3, it is clear that these arguments have no merit.

It has been decided in innumerable decisions in this court that with reference to bankruptcy distribution there are only two classes of creditors—

(1) Those entitled to be paid in full as priority creditors, and—

(2) Those creditors who are entitled to equal distribution after priority claims have been paid.

The courts have many times held that secured creditors and unsecured creditors both are within the second class of creditors and that no evidence need be introduced by a trustee in bankruptcy as to distributions which could be made to secured creditors as opposed to unsecured credi-

tors, since no such difference in distribution in bankruptcy exists.

Hassock v. *Varick Bank,* 206 U.S. 28.
Swartz v. *Fourth National Bank,* 117 Fed. 1 (C.C.A. 8th).
Livingston v. *Heineman,* 120 Fed. 786.
Gorman v. *Wright,* 136 Fed. 164.

And even if we assume as a matter of argument that a secured creditor is in a different class from an unsecured creditor with respect to the issues herein raised, it is clear that the petitioner in this case is not a secured creditor, for it has also been decided that a creditor whose claim is secured by one or more third persons is not a secured creditor and is in the same class as one who is not so secured. Chapter 1, section 1, sub-section 23, of the Bankruptcy Act states that a " 'secured creditor' shall include a creditor who *has security for his debt upon the property* of the bankrupt of a nature to be assignable under this act, or who owns such a debt for which some indorser, surety, or other persons secondarily liable for the bankrupt *has such security upon the bankrupt assets.*"

Swartz v. *Fourth National Bank of St. Louis,* 117 Fed. 1.
Livingston v. *Heineman,* 120 Fed. 786.
Gorman v. *Wright,* 136 Fed. 164.
In re H. V. Keep Shirt Co., 200 Fed. 80.

From the record of the case, no evidence appears to show that the petitioner has any security for his debt upon the property of the bankrupt or that the guarantor secondarily liable had any such security upon the bankrupt assets, so that the above rulings apply.

The argument of the petitioner that no evidence was submitted as to what dividends were paid to creditors

generally, your respondent submits, is not open at this time, as the court has found as a fact that it was preferred over other creditors of the same class, but for the purpose of argument your respondent says that the undisputed evidence of the president of the bankrupt corporation as to the assets and liabilities of the bankrupt corporation on January 14, 1933, the date of the filing of the involuntary petition, to the effect that the total assets were $3000 at market value and current liabilities $14,900, was sufficient to support any burden of proof resting on the respondent on this issue since it established what the possible distribution before deducting administration expenses would be.

II.

THE TRIAL COURT'S FINDINGS OF FACT AS SUPPORTED BY THE EVIDENCE APPEARING IN THE RECORD BEFORE THIS COURT RENDERED THE PETITIONER'S REQUEST FOR RULING No. 8 IMMATERIAL, AND THEREFORE THE RULING BY THE TRIAL JUSTICE REFUSING TO GRANT THIS REQUEST, EVEN IF IT WERE AN ERRONEOUS RULING, WAS NOT PREJUDICIAL TO THE PETITIONER, AND GIVES HIM NO RIGHT TO A REVIEW OF THE QUESTION OF LAW PRESENTED BY THIS REQUEST FOR RULING.

The record in this case (see page 12) indicates that the payments which were ordered returned by the petitioner to the respondent as preferential were all received by the petitioner between November 25, 1932, and January 3, 1933. (See Record, page 12.) The record also contains (see pages 15 and 16) two balance sheets of the Metropolitan Builders Supply Company as of December 1, 1932, and November 1, 1932. The uncontradicted evidence as to the fair market value of the assets on these dates indicates that on December 1, 1932, the current assets at a fair value amounted to $7335.57, and that the current liabilities were

$13,648. (See Balance Sheet, Record, page 15.) Even if we assume that the rule of law requested by the petitioner, to the effect that the respondent had the burden of proving that at the time of each payment the petitioner received more than other creditors of the same class could have received if the assets had at that time been distributed, is correct, it appears clear that the petitioner did receive such preferential treatment. At best, if the assets had been distributed on November 1, 1932, almost thirty days prior to the first payment to the petitioner in this case, the payment to creditors of the same class would not have been larger than approximately 74%. If the assets had been distributed as of December 1, 1932, the creditors of the same class as the petitioner would have received approximately 57% of their claims. If the assets had been distributed on or about January 14, 1933, the testimony appearing in the record on page 8 indicates that the creditors would have received approximately 20%. It appears clear that the assets of this company were shrinking with rapidity.

Since the record indicates that the payments were made to the petitioner between November 25 and January 3, 1933 (see Record, page 11, line 10, and also page 12), it would appear fair in arguing this case to use the average figure as shown by these balance sheets to have been the proportionate ratio of assets to liabilities on November 1, 1932, December 1, 1932, and January 14, 1933, as a basis for computation. This figure is approximately 50%. The payments were grouped so closely that over $1500 of the total $1688.96 was paid between November 25 and December 29, 1932.

So that, even if we assume that the trial justice should have granted request for ruling No. 8 even though it was directly in conflict with the decision of the Supreme Court of Massachusetts as laid down in the case of *Rubenstein* v.

Lottow, 223 Mass. 227, the finding in this case would have been the same. How, then, was the petitioner prejudiced by the failure to grant this request?

Certainly it would appear in accordance with all principles of justice and good sense to hold that the refusal by the court to grant a request for a ruling rendered immaterial by the court's findings of fact should not be ground for overturning a decision arrived at after a hearing and a mature consideration of all the facts. And the law appears to support such a conclusion.

Section 269 of the Judicial Code of the United States (Act of March 3, 1911, c. 231, 36 Stat. 1163, as amended February 26, 1919, c. 48, 40 Stat. 1181), declares: "On the hearing of any writ of error, civil or criminal, the court shall give judgment after an examination of the entire record before the court without regard to technical errors, defects or exceptions which do not effect the substantial rights of the parties."

The principle here enunciated is a statutory codification of the common-law rule commonly referred to as the "Rule of Substantial Justice."

This rule is enunciated in many cases and is based on the principle that, even though an error of law or procedure was committed in the conduct or disposition of a case, if substantial justice was done the parties and the error was immaterial or technical, the finding should be allowed to stand.

Eau Claire National Bank v. *Jackman,* 204 U.S. 522, 534, *et seq.*

Virginia R.R. & Power Co. v. *Smith & Hicks, Inc.,* 105 S.E. 532 (Va.)

Green v. *Ruffin,* 125 S.E. 742.

West v. *United States,* 258 Fed. 413.

Ashapa v. *Reed,* 280 Mass. 514, at 516.

Gigoux v. *Henderson*, 107 Kans. 325.
Queeney v. *Willis*, 225 N.Y. 374.
Stevens v. *Ross*, 1 Calif. 94, at 98.

The respondent respectfully submits that, since this court on certiorari need only exercise its jurisdiction to review when, in its discretion, the case merits review, substantial justice having been done the petitioner, the sound exercise of its discretion should result in its denying this petition.

III.

THE DECISION OF THE SUPREME JUDICIAL COURT OF MASSACHUSETTS IN THIS CASE WAS IN ACCORDANCE WITH THE SPIRIT AND PURPOSE OF THE BANKRUPTCY ACT, AND IS SUPPORTED BY DECISIONS OF THIS COURT AND THE WEIGHT OF AUTHORITY IN THE UNITED STATES DISTRICT COURTS, CIRCUIT COURTS OF APPEAL, AND THE HIGHEST COURTS OF THE STATES.

The elements necessary to establish a voidable preference under the Bankruptcy Act are (1) a transfer of the property of the debtor without present consideration, (2) insolvency at the time of the transfer, (3) the securing by the creditor of an excessive percentage of his debt in enforcing the transfer, and (4) reasonable cause on the part of the creditor then to believe that the enforcement of such transfer would effect a preference.

The findings of fact of the trial court establish (and they are not contested by the petitioner) that the Metropolitan Builders Supply Company was insolvent at the time of the receipt of the payments by the petitioner; that it gave no new consideration at that time; that it then had reasonable cause to believe that it was securing a preference. The petitioner argues, however, that the further finding

made by the court that the "payments made thereafter did effect a preference over other creditors of the same class" was based on an interpretation of the Bankruptcy Act by the Supreme Court of Massachusetts as set forth in the case of *Rubenstein* v. *Lottow*, 223 Mass. 227; that this decision was incorrect and should not have been followed by the Municipal Court of the City of Boston, as it was in conflict with the decisions of the Circuit Court of Appeals for the Eighth Circuit. The petitioner argues that the issues thereby presented are as follows:

> "(1) Whether the preferential character of a transfer of property is to be determined as of the date of the actual transfer, or as of some future time, viz., the time of the filing of the petition in bankruptcy.
>
> "(2) What is the test to be applied in determining whether a creditor, who is alleged to have received a preferential transfer, has received a greater percentage of its debt than other creditors of the same class:
>
> "(a) What percentage creditors of the same class could have received at the date of the actual payment or transfer, or
>
> "(b) What other creditors of the same class received at some future time, viz., the time of the filing of the petition in bankruptcy or final administration of the bankrupt estate."

The respondent respectfully submits that the petitioner's statement of the supposed questions at issue is based on an erroneous assumption of fact, the absence of which fact destroys whatever argument the petitioner may have. The assumption made by the petitioner in its statement of the questions is that it assumes as a fact that, when the petitioner (or any creditor in any bankruptcy) receives a

payment on account within four months, it thereupon surrenders all rights to receive any further payments from the debtor or, in the event of bankruptcy, a dividend from the estate; in other words, that the partial payment on account is in full settlement of the claim as would be the case in bankruptcy distribution. This obviously is not so.

In order to make this point clear, the respondent submits to the court the following theoretical case:

Let us assume that a voluntary or involuntary petition in bankruptcy was filed against a corporation or individual on July 2, 1935. Let us assume further that a trustee in bankruptcy is appointed and brings a suit to recover a payment in the sum of $500 made to a creditor the day before the petition was filed. Let us assume that the court finds as a fact that the creditor's claim against the bankrupt on July 1st was $1000; that the debtor owed the creditors of the same class as the creditor who received the payment the sum of $10,000; and that the fair value of its assets as of July 1st was $5000. Let us further assume that the court has found as a fact that at the time of the payment the debtor was insolvent and that the creditor had reasonable cause to believe that it was securing a preference. On this set of facts the petitioner would argue that the trustee in bankruptcy could not recover the sum of $500 paid to the creditor, since it received but 50% of its claim and since at the time of the payment all creditors could have received 50% of their claims. Therefore, the petitioner argues, this creditor was not preferred.

It appears clear to the respondent that what is overlooked in this argument is that the $500 received by the creditor was not in payment of its full claim, but merely payment in full of that portion of its claim to which that $500 was applied and that it still has remaining to it the right to collect the remaining $500 from the debtor or, in the event of bankruptcy, to prove its claim for $500. Assume fur-

ther that the creditor after bankruptcy does file a proof of claim for $500 and it is fair to assume that at least a dividend of 30% will be paid to creditors after deduction of administration expenses. Thus this creditor would receive $500 before bankruptcy and $300 in bankruptcy, making a total of 80% of its $1000 claim, whereas all other creditors would receive a dividend of 30% of the same multiple of $1000.

This example is not as strong a case as the instant case, as in this case the creditor before bankruptcy received full payment of its account.

The mathematical argument above made is used as a basis for the decisions in the cases about to be cited.

In the case of *Bronx Brass Foundry Inc.* v. *Irving Trust Co.*, 76 Fed. (2d) 935 (C.C.A. 2d) the precise question argued by the petitioner in this case in its behalf was therein presented by the appellant. The court stated, in denying relief to the appellant, that "Whether a creditor of an insolvent has received an unlawful preference is not to be determined by what the situation would have been if the estate had been completely liquidated and distributed among all the creditors at the time when the alleged preferential payment was made, but upon whether the ultimate result of a payment by a known insolvent will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class."

In the case of *Commerce Guardian Trust Co.* v. *Devlin*, 6 Fed. (2d) 518, the court again refused to follow the argument as made by the petitioner in this case. The facts in that case were that on November 18, 1921, the bankrupt owed the creditor more than $14,000 for money loaned beginning in August, 1921. A petition in bankruptcy was filed on January 6, 1922, and adjudication was made on January 22, 1922. The assets of the bankrupt were found

to be approximately $12,000 and liabilities $25,000 on November 18th and November 30th, the dates on which payments were made. The bankrupt received a total of $6300 on these two dates. Counsel for the bank argued that, since the bank did not receive a greater proportion of its debt than other creditors could have received at the time of distribution, it had not been preferred. The court said in part:

> "We see no merit in the suggestion that the Bank got no greater percentage of its own claim (about 48%) than creditors generally would have had if we accept the estimates of the bookkeeper of 50%. The bank actually received 100% on $6,300. of its claim and if the preference were withheld would be entitled to receive on the balance of its claim the same percentage as other creditors of its class."

Although neither the petitioner nor the respondent in preparing their respective briefs for the Supreme Court of Massachusetts cited a decision on the point in issue, and although the Supreme Court of Massachusetts stated that it had been unable to find a decision, it appears to the respondent that this question has been decided by this Honorable Court in the case of *Eau Claire National Bank v. Jackman,* 204 U.S. 522, which case has recently come to his attention. In that case the petitioner alleged that the Supreme Court erred in the following particulars among others:

(*a*) In holding that a transfer made within four months of the bankruptcy proceedings, which enabled a creditor to receive any portion of his debt, constituted a preference.

(*b*) That although the effect of the transfer in question did not operate to give back a greater percentage of its debt than other creditors of the same class, such transfer constituted a preference.

The court's decision with reference to these arguments of counsel for the bank in part is as follows:

> "Their fundamental contention is that the transfers to the bank were not invalid as a preference if their enforcement would not operate to give the bank a greater percentage of its debt than other creditors of the same class would receive. And such, it is further contended, was not the result, and it is intimated that claims of possible and fictitious creditors were in effect considered. But this contention encounters the fact found by the jury and the trial court. We have already seen what, in the opinion of the trial court, the evidence established as to the effect of the transfers, and the jury found that Young was insolvent at the time they were made, and that the purpose of their execution was to give the bank a preference and to enable it to obtain a greater percentage of its debt than other creditors of Young of the same class. These findings were not disturbed by the Supreme Court, and we must accept them as stating the facts established by the evidence, although counsel seem to invoke an examination by us of the record against them. Taking them as true, they show a case of preference and grounds to set it aside."

Throughout the discussion in the above-cited case it appears to be assumed that the distribution referred to by the Bankruptcy Act is the distribution which would be secured by creditors out of the assets of the bankrupt estate, and not what amount could have been received by other creditors at the time of distribution. Cases too numerous to cite can be given in support of the decisions of the Supreme Court of Massachusetts which are contrary to the argument of the petitioner.

Baker v. *Chisholm,* 268 Mass. 1, at 7.

Rubenstein v. *Lottow*, 223 Mass. 227.
LaTrobe v. *Cross*, 29 Fed. (2d) 210.
Williams v. *Bank of America Nat. Assoc.*, 55 Fed. (2d) 884.
Swartz v. *Fourth National Bank*, 117 Fed. 1, at 7.
In re Watkinson, 146 Fed. 142.
In re Mayo Contracting Co., 157 Fed. 469.
In re Carlton Export & Import Co., 121 Fed. 663.
Cohen v. *Goldman*, 250 Fed. 599.
In re Star Spring Bed Co., 265 Fed. 133.
Eyges v. *Boylston National Bank*, 294 Fed. 286.

In the case of *Swartz* v. *Fourth National Bank*, 117 Fed. 1, the court said in part:

> "The statement of these facts is in itself a demonstration that if the Bank can retain this money and procure the allowance of the balance of its claim, it will receive a greater percentage of its debt out of the estate of the insolvent than other creditors of its class who receive no such payment."

Apart from the arguments of law already given supporting the rule of law adopted by the Supreme Judicial Court of Massachusetts, and followed in this case, there are numerous practical arguments to be advanced in its favor. It would place an almost insurmountable hurdle in the way of a trustee in bankruptcy to call upon him to prove that creditors at the time of each payment could not have received the same proportionate distribution that the preferred creditor did receive. Obviously, in bankruptcy, the records of assets and liabilities are not too easily available.

Furthermore, it might prevent the recovery of any preference. Suppose a creditor were to receive over a period

of thirty days just prior to bankruptcy payments daily of $100, and let us assume that its total claim was $3000, so that it received payment in full, and let us suppose further that the assets of the debtor during the month prior to bankruptcy, during which these payments were made, were sufficient to pay all creditors 50 cents on the dollar: Would the petitioner have the court refuse relief to the trustee in bankruptcy because at the time of each payment the creditor had received but 3⅓% of its claim? The very words of the Bankruptcy Act indicate no such intention. As stated by the Supreme Court of Massachusetts in the case of *Rubenstein* v. *Lottow*, 223 Mass. 227: "The pertinent words of the bankruptcy act . . . express futurity. Whether 'the effect of the enforcement' of the transfer 'will be to enable' one creditor to get a larger percentage of his debt than other like creditors, by implication reaches forward to a time when an authoritative distribution can be made." "The interpretation urged would result in inequality of distribution of the debtor's assets among his creditors. Equality of distribution is one of the fundamental objects of a bankrupt law."

The only reason advanced by the petitioner for this court's taking jurisdiction is that there is apparent conflict between the rule as set forth in Massachusetts and the rule as set forth by decisions of the Federal District Court of Kansas and Arkansas and the Circuit Court of Appeals of the Eighth Circuit. The petitioner claims further that the decision of the Circuit Court of Appeals of the Eighth Circuit is supported by the great weight of authority.

The respondent submits that there is no conflict between the cases, but, if there is a conflict, that the great weight of authority supports his contentions.

One of the most quoted cases in the law of preferences is that of *Swartz* v. *Fourth National Bank*, 117 Fed. 1. It

will be observed that this case was decided in the Circuit Court of Appeals for the Eighth Circuit. In that case the court said in part:

> "The statement of these facts is in itself a demonstration that if the Bank can retain this money and procure the allowance of the balance of its claim, it will receive a greater percentage of its debt out of the estate of the insolvent than other creditors of its class who receive no such payment. . . . The dominant purpose of the prohibition of a preference was not to benefit or injure, or to prevent the benefiting or injuring of any creditor or class of creditors, but to prevent the debtor from making any disposition of his property which would prevent its equal distribution—to prevent him from doing anything which would result in payment out of his property of a larger percentage upon any claim than others of the same class would receive. The plain intention of Congress and the legal effect of the paragraph (60a) was to make *every* transfer of any of the insolvent's property by means of which a larger percentage would be paid out of his estate to any creditor on any claim than every other creditor and every other claim of the same class would receive, a preference to be surrendered or avoided under the other provisions of the Statute" (60b).

The leading case, and one of the three cases cited by the petitioner in support of his argument, is that of *W. S. Peck & Co.* v. *Whitmer* (C.C.A. 8), 231 Fed. 893. That case cited with approval the case of *Swartz* v. *Fourth National Bank.* It does not support the petitioner's argument, but appears to the respondent, on the contrary, to support his argument. The question there decided was that on the facts of that particular case the trustee had failed to prove

the essential element found as a fact here, which is a necessary element of proof in every preference case, that is, that at the time of the receipt of the payments the debtor had reasonable cause to believe it was securing a preference. The court stated:

> "Taking the record as it stands, how could the appellant be held to have believed that if the estate of the bankrupt had been distributed at the time of the payments it would not have given every creditor a greater percentage of their debt than they were receiving? *The creditor who receives a partial payment on his debt, so far as the question of his having reasonable cause to believe that the enforcement of the payment would effect a preference, has a right to look at the bankrupt estate at the time payment is made.*"

The argument of the respondent as to the meaning of the finding in *Peck & Co.* v. *Whitmer,* is supported by a statement made in Gilbert's Collier on Bankruptcy (Third Edition), page 881, as follows:

> "The decision of Peck & Company vs. Whitmer is stated to be that on the particular facts of the case the creditor at the time they received the payment did not have reasonable cause to believe that a preference would result therefrom."

The case next cited by the petitioner in support of its argument is that of *Mansfield Lumber Co.* v. *Sternberg* (C.C.A. 8), 38 Fed. (2d) 614. Here again the court cites with approval the case of *Swartz* v. *Fourth National Bank,* (see *supra*). Here again the decision is based on a set of facts peculiar to that case. There the creditor received a total of 7.79% of its claim *and executed a general release.* The assets of the bankrupt paid to general creditors of the

same class 11%. It will be observed that the debtor here settled its entire claim for 7.79% and did not retain the right to prove the balance of its claim in bankruptcy. The court therefore found that "There was a failure of proof on the part of the Trustee that the transfer operated as a preference."

The last case cited by the petitioner in support of its argument is that of *Haas* v. *Sachs* (C.C.A. 9), 24 Am. B.R. (N.S.) 388. That case again cites with approval the earlier cases which your respondent submits do not sustain the petitioner's argument. Your respondent submits that the decision is not a clear one, and that, moreover, it contains a vigorous dissent.

It would appear, therefore, that the rule in the Eighth Circuit, at least until the confusing decision in the case of *Haas* v. *Sachs,* was in accordance with the decisions of every other circuit and with the great weight of authority. Without having cited any other cases, the petitioner would argue that the great weight of authority supports its argument. The respondent submits that the only case which the petitioner can quote which is apparently in support of its petition is that of *Haas* v. *Sachs,* which apparently conflicts with the decisions in every other Circuit Court of Appeals, and the great weight of authority in the federal courts and in the state courts. The respondent also submits that the case of *Haas* v. *Sachs* is not a clear decision and is in conflict with earlier rulings of the same circuit.

In commenting on the rule advanced by the petitioner, Judge Lowell, in the case of *Eyges* v. *Boylston National Bank,* 294 Fed. 286, stated:

> "This rule, however, has never been applied so far as I am aware, except where at the time of trial of the suit for an alleged preference it was clear that the same percentage would be paid to other creditors as to the one against whom the suit is brought."

The argument on which the petitioner places great weight in its brief to the effect, that, unless this court decides this question on this petition, business concerns will be left in "utter confusion," has little to support it. Apart from the fact that the respondent believes that the rule of law in question has already been settled in the case of *Eau Claire National Bank* v. *Jackman,* 204 U.S. 522, the principle enunciated by the Supreme Court of Massachusetts and sought for by the respondent is firmly settled by the great weight of authority.

The recovery of a preference is a proceeding which necessarily arises after the deed is done. Creditors who receive payments on account certainly do not do so, and have no obligation to do so, with their eyes directed toward the recovery of the payment by a possible subsequent trustee in bankruptcy. They have a valid claim and are entitled to receive whatever payments they can secure as they go along. The Bankruptcy Act, in order to effectuate equal distribution among creditors within four months, serves to make them return what they would otherwise be properly entitled to. How, then, can the rule of law in this case affect the course of conduct of a business man? He is entitled to secure his payments and will do so whatever rule be enunciated. The only person who will be guided is the trustee in bankruptcy. As to trustees, the respondent submits that they long have proceeded under the assumption that the rule urged by the respondent was established beyond question.

Conclusion.

While the respondent does not rely upon the jurisdictional argument to the effect that the petitioner has filed his application late, it appears to him that this argument is a sound one and that this petition should be dismissed on this preliminary ground.

If, however, the court is of the opinion that it has been applied for in time, then the respondent respectfully submits that it should be denied because (1) the ruling of law made at the trial, the correctness of which is the only issue raised by the petitioner in its brief, was immaterial and did not affect its substantial rights; (2) if it was not immaterial, the respondent submits that the ruling is in accordance with the law as decided in this court and with the great weight of authority in the federal and state jurisdictions which have been called upon to pass on the question herein submitted.

The respondent therefore respectfully prays that the petition for writ of certiorari be denied.

Respectfully submitted,

MATTHEW BROWN, Trustee in Bankruptcy of Metropolitan Builders Supply Company,

By his Attorneys,

Harrison J. Barrett,

Matthew Brown.